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IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

No. 79-1836

KENNETH LEO FOWLER AND FLORA D. FOWLER,
Petitioners,

v.

GENERAL DEVELOPMENT CORPORATION,
Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

BRIEF FOR RESPONDENT IN OPPOSITION

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OPINIONS BELOW

The opinion of the United States Court of Appeals for the Fourth Circuit is unreported. That opinion is printed in the Appendix to the Petition for Certiorari.[1] A copy of the oral opinion rendered by United States District Judge Frank A. Kaufman, granting partial summary judgment, is reproduced in the Appendix to this Brief for Respondent in Opposition.[2] The memorandum and order and judgment

[1] The Appendix to the Petition for Certiorari will be referred to by the reference "Pet. App.".

[2] The Appendix to Respondent's Brief will be referred to by the reference "Res. App.".

of the district court are included in the Appendix to the Petition.

JURISDICTION

The jurisdictional requisites are adequately set forth in the Petition.

QUESTION PRESENTED

Should the Supreme Court review the decisions of the district court and court of appeals below as to specific facts, evidentiary rulings and application of state statutes of limitations, when those decisions are consistent with this Court's holdings in claims brought under the Securities Exchange Act of 1934, with the Federal Rules of Evidence and with Maryland law?

STATUTES INVOLVED

The statutes involved are adequately set forth in the Petition.

STATEMENT OF THE CASE

Petitioners filed suit in the United States District Court for the District of Maryland on July 25, 1975, against Respondent, combining in their complaint a count of common law fraud with a count asserting fraud allegedly arising under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j (1976), and Rule 10b-5. The claims of fraud arose from Petitioners' purchase from Respondent of two unimproved lots of real property located in Florida, and the negotiations for the construction by Respondent of a house for Petitioners.

Petitioners executed contracts with Respondent in April, 1969, to purchase two lots in Greater Port Charlotte, Florida, a community of over 35,000 located on the West Coast of Florida. The contracts called for initial downpay-

ments and subsequent monthly installments. Petitioners claimed that misrepresentations were made to them in 1969 concerning the location of their two lots. Thereafter, an agreement was reached, in August, 1970, to exchange those lots originally purchased for two lots in another location. Petitioners further claimed that at the time of the August, 1970 exchange of lots, they were told falsely that there would be a sewer line to the lots when they were ready to build a house or houses on one or both of the lots. The installment payments called for under the original contracts were completed by Petitioners.

Further negotiations were conducted in 1973 toward an agreement under which Respondent would build a house for Petitioners on another lot, not the subject of the earlier contracts. Petitioners claimed misrepresentation as to the price and other terms of the proposed agreement for construction of their house. Agreement for the construction of the house was never reached.

Petitioners thus claimed common law fraud and securities act violations for the alleged April, 1969, misrepresentation as to the location of the two lots, for the alleged April, 1970, misrepresentation as to the presence of sewers, and for the alleged June, 1973, misrepresentation as to the price and terms for the construction of a house. By special verdict questions submitted to the jury at the conclusion of a five day trial, Respondent was exonerated of any fraud in each of the three separate instances. The special verdict of the jury further stated that Petitioners should have discovered the alleged 1970 fraud prior to three years before the institution of the suit.

Prior to trial, the district court below granted Respondent's motion for partial summary judgment, dismissing Petitioners' count of securities fraud, ruling that the contractual rights acquired by them did not constitute a "security" (Res. App. p. 1a). The district court filed a

memorandum and order at the conclusion of trial, accompanying the judgment entered in accordance with the jury's special verdict, reaffirming its earlier dismissal of the securities fraud count. The district court's memorandum and order further provided that even had the rights acquired by Petitioners constituted a "security", the cause of action based upon the Securities Exchange Act of 1934 was barred by limitations (Pet. App. p. 24). The United States Court of Appeals for the Fourth Circuit affirmed, *per curiam*.

ARGUMENT

INTRODUCTION

Petitioners propose that this Court review specific evidence and factual issues. Actually, Petitioners want this Court to substitute its judgment for that of the jury, district court and court of appeals below when, in fact, there is an absence of national import and no reason for this Court to grant certiorari in this primarily local matter. It is inappropriate to seek this Court's review of essentially evidentiary questions and concurrent findings of fact by two courts below. Accordingly, the Petition should be denied. *International Brotherhood of Electrical Workers v. Foust*, ____ U.S. ____, 99 S. Ct. 2121, 2124 n.7 (1979); *Berenyi v. District Director, Immigration and Naturalization Service*, 385 U.S. 630, 635-36 (1967); *Graver Tank & Manufacturing Co. v. Linde Air Products Co.*, 336 U.S. 271, 275 (1949).

Hereafter, Respondent will reply directly to the arguments advanced by Petitioners commencing with the heading "Reasons For Granting The Writ" (Pet. p. 27), adopting, for convenience, the same numerical order used by Petitioners.

I.

NO CONFLICT EXISTS IN DETERMINING WHAT IS A SECURITY IN THE INTERSTATE SALE OF UNIMPROVED REAL PROPERTY AND THE DECISION BELOW IS FULLY CONSISTENT WITH *ERNST & ERNST V. HOCHFELDER*, 425 U.S. 185, *reh'g denied*, 425 U.S. 986 (1976).

Petitioners' complaint that there is confusion and conflict as to the meaning of "investment contract" and "security" in the context of the interstate sale of unimproved real property is misplaced. There exists no confusion or conflict in the federal courts. Petitioners' argument to the contrary is simply the first of repeated efforts to have this Court review factual issues properly resolved below.

Petitioners ignore the fact that the jury, when presented with evidence of the three alleged frauds, returned a verdict in favor of Respondent as to each. The court of appeals below affirmed, stating, "The record clearly supports a determination by the jury that the Fowlers did not meet their burden to establish all the elements necessary to make out a deceit action" (Pet. App. pp. 22-23). Since the evidence presented as to the common law fraud count was the same evidence of the Petitioners' claim of securities fraud, a similar result would have obtained had the claim of securities fraud been submitted to the jury. Common law and securities fraud causes of action share similar proof requirements, including the proof of scienter in an action for civil damages under § 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5. *Ernst & Ernst v. Hochfelder*, 425 U.S. 285, *reh'g denied*, 425 U.S. 986 (1976); *Wedeman v. City Chevrolet Co.*, 278 Md. 524, 366 A.2d 7 (1976). The jury decided none existed.

Moreover, Petitioners ignore the proper application of a one year limitations period which bars their § 10(b) claim. It was uncontradicted that Petitioners had knowledge of the alleged April, 1969 fraud prior to July 24, 1972. With

respect to the fraud alleged to have taken place in April, 1970, the jury, in answer to a special question, found that Petitioners, by the exercise of reasonable diligence or care, should have known of that alleged fraud on or before July 24, 1972. There existed no dispute that Petitioners had knowledge of the allegedly fraudulent 1973 conduct in 1973, and well before July 25, 1974 (one year preceding the filing of the action). Since no statute of limitations is provided for civil actions under § 10(b), District Judge Kaufman, in accordance with this Court's holding in *Ernst & Ernst, supra,* at 425 U.S. 210 n.29, applied the analogous one year Maryland statute of limitations contained in The Maryland Securities Act, *Corporations & Associations Article* of the Maryland Code, §§ 11-101, 703 (1975) (subsequent amendments to the Act, effective July 1, 1976, and after filing of the instant action, inapplicable). *Fox v. Kane-Miller Corp.*, 542 F.2d 915, 918 (4th Cir. 1976). The court of appeals approved accordingly, stating, "the district judge was beyond any doubt correct" in holding that the one year statute of limitations barred any Securities Exchange Act claims (Pet. App. p. 5).

With the preceding fully in mind, Respondent now turns briefly to Petitioners' claim that confusion and conflict exist among the federal courts. Petitioners are simply wrong. There exists no conflict or confusion in determining when interstate sales of undeveloped real property constitute "investment contracts" and, thus, a security within the meaning of the Securities Exchange Act of 1934. *SEC v. W.J. Howey Co.*, 328 U.S. 293, 298-99 (1946). Apparently, in pressing their argument, Petitioners would have this Court discard the guiding principles for determining what is an investment contract established in *Howey*.

In passing both the Securities Act of 1933, 15 U.S.C. § 77a (1976), and the Securities Exchange Act of 1934, 15 U.S.C. § 78a (1976), Congress did not attempt to identify or

provide a test by which transactions are to be considered securities, leaving that task to the federal courts and Securities Exchange Commission. This Court has recognized that the test of what is an "investment contract" under the 1933 Act and 1934 Exchange Act is the same and turns largely on the facts of the particular transaction under scrutiny. The test "embodies a flexible rather than a static principle, one that is capable of adaptation." *Howey, supra,* at 328 U.S. 299. "[F]orm should be disregarded for substance and the emphasis should be on economic reality." *Tcherepnin v. Knight,* 389 U.S. 332, 336 (1967); *see United Housing Foundation, Inc. v. Forman,* 421 U.S. 837 (1975).

No new test need be crafted solely for transactions involving the interstate sale of real property as Petitioners suggest. The *Howey* principle has become a "sacred measure"[3] in determining the existence of a security and is as appropriate today in transactions involving the interstate sale of Florida real estate as it was at its creation, in 1946. The *Howey* test arose from a factual setting which involved a somewhat different sale of Florida real estate:

> [A]n investment contract for purposes of the Securities Act means a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third-party, it being immaterial whether the shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed in the enterprise. 328 U.S. at 298-99.

The definition of an "investment contract" — with its four elements of (1) an investment of money (2) in a common enterprise (3) for profit and (4) generated from the efforts of others — has, recently, been fully considered and

[3] *Braniff Airways, Inc. v. LTV Corp.,* 479 F. Supp. 1279, 1284 (N.D. Tex. 1979).

reaffirmed by this Court in *International Brotherhood of Teamsters v. Daniel*, 439 U.S. 551 (1979), and, earlier, in *Forman*, wherein Mr. Justice Powell stated, at 421 U.S. 837, 852:

> This test, in shorthand form, embodies the essential attributes that run throughout all of the Court's decisions defining a security.

Moreover, this Court, in *Forman*, has spoken to the applicability of the *Howey* test in determining the presence of an investment contract in transactions involving residential real estate. It has been firmly established that if residential real estate represents an asset to be developed or occupied by the purchaser, rather than an investment to be managed by the efforts of others, the real estate transaction does not constitute an investment contract. *Forman, supra*, at 421 U.S. 858.[4]

[4] This Court, in *Forman, supra*, at 421 U.S. 859 n.26, expressed unwillingness to extend securities laws to real estate transactions.

> Moreover extension of the securities laws to real estate transactions would involve important questions as to the appropriate balance between state and federal responsibility. The determination of whether and in what manner federal regulation may be required for housing transactions, where the characteristics of an investment in securities are not present, is better left to the Congress, which can assess both the costs and benefits of any such regulation.

A review of the legislative history of the Interstate Land Sales Full Disclosure Act, 15 U.S.C. §§ 1701-1720 (Supp. 1975-1979), reveals that while it was designed to provide purchasers of real estate with virtually all of the securities law safeguards, Congress expressly declined to give the SEC regulatory control over its enforcement. *Hearings on S. 275 before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 90th Cong., 1st Sess. 211 (1967); Berman & Stone, *Federal Securities Law and Sale of Condominiums, Homes and Homesites*, 30 Bus. Law. 411 (1975).

The Securities Exchange Commission, through Securities Act Release No. 5347, January 4, 1973, similarly concluded that the offer of real estate, without any collateral arrangements with the seller or sellers, does not involve the offer of a security.

What the Petitioners attempt to foist on this Court as conflict among federal courts with respect to the definition of a security in an interstate land sale setting is, actually, the product of proper application of the *Howey/Forman* principles to the facts peculiar to the individual transactions in issue in the various cases. What Petitioners term as "mixed" results in such cases (Pet. p. 31) are simply results dictated by application of the proper law to different facts. There exists no controversy as to the principle of law to be applied. *E.g., De Luz Ranchos Investment, Ltd. v. Coldwell Banker & Co.*, 608 F.2d 1297 (9th Cir. 1979); *Cameron v. Outdoor Resorts of America, Inc.*, 608 F.2d 187 (1979), *aff'd in part, vacated and remanded in part*, 611 F.2d 105 (5th Cir. 1980); *Woodward v. Terracor Corp.*, 574 F.2d 1023 (10th Cir. 1978); McCown v. Heidler, 527 F.2d 204 (10th Cir. 1975); *Fogel v. Sellamerica, Ltd.*, 445 F. Supp. 1269 (S.D.N.Y. 1978); *Timmreck v. Munn*, 433 F. Supp. 396 (N.D. Ill. 1977); *Davis v. Rio Rancho Estates, Inc.*, 401 F. Supp. 1045 (S.D.N.Y. 1975); *Happy Investment Group v. Lakeworld Properties, Inc.*, 396 F. Supp. 175 (N.D. Cal. 1975); *Contract Buyers League v. F & F Investment*, 300 F. Supp. 210 (N.D. Ill. 1969), *aff'd sub nom, Baker v. F & F Investment*, 420 F.2d 1191 (7th Cir. 1970).

District Judge Kaufman properly applied the *Howey/Forman* principles to Petitioners' transactions which involved solely the purchase of lots and negotiations for the construction of a house, without any collateral arrangements with Respondent. He ruled that the transactions did not constitute the sale of a security and, in granting partial summary judgment, dismissed the securities count (Res. App. p. 1a). That ruling was reaffirmed by the district judge upon his review of all the evidence at the conclusion of trial (Pet. App. p. 24).

This Court, however, like the court of appeals below, need not concern itself with that altogether proper ruling.

No review of the securities issue is necessary, in light of the jury's verdict below and evidence reviewed on appeal. Respondent was absolved of all liability for the alleged frauds and Petitioners' securities claims were barred by limitations, in any event.

II.

THE DECISION BELOW IS NOT IN CONFLICT WITH MARYLAND LAW AND HAS NO NATIONAL SIGNIFICANCE.

The Petitioners attempted below to deny Respondent its limitations defenses on the basis of Maryland Code, *Courts & Judicial Proceedings Article,* § 5-204 (1980):

> A foreign corporation required by law to qualify or register to do business in the State or a person claiming under the corporation, may not benefit from any statute of limitations in an action at law or suit in equity:
>
> (1) Arising out of a contract made or liability incurred by the corporation while doing business without having qualified or registered; or
>
> (2) Instituted while the corporation is doing intrastate or interstate or foreign business in the State without having qualified or registered.

The crux of the issue presented to both the district court and court of appeals below was: Did Respondent have to qualify or register to do business in Maryland? The district court, affirmed by the court of appeals below, ruled that Respondent was engaged solely in the solicitation of interstate sales and did not need to register or qualify. As such, the sanction contemplated by § 5-204 of the *Courts & Judicial Proceedings Article* of the Maryland Code did not apply. The limitations defense was available to Respondent.

Petitioners, as they did below, have confused what constitutes "doing business" for the purposes of subjecting

a foreign corporation to a court's *in personam* jurisdiction with what constitutes "doing business" for purposes of requiring a foreign corporation to register or qualify. Petitioners blur decisions from the Court of Appeals of Maryland dealing with the imposition of *in personam* jurisdiction with that court's decisions dealing with the requirement of registration or qualification, and sanctions imposed for failing to register or qualify.

In rendering its *per curiam* affirmance, it was unnecessary for the appellate court to repeat the uncontroverted facts establishing that Respondent's Maryland activities were purely directed to solicitation of sales interstate in character, namely, the sale of land and/or houses in Florida. The court of appeals then confirmed the district judge's analysis of applicable Maryland law that the mere solicitation of interstate sales does not constitute "doing business" for the purpose of Maryland statutes requiring qualification or registration before doing intrastate, interstate, or foreign business.[5] That analysis of Maryland law is consonant with the holdings of the Court of Appeals of Maryland. *E.g., S.A.S. Personnel Consultants, Inc. v. Pat-Pan, Inc.*, 286 Md. 335, 407 A.2d 1139 (1979); *G.E.M., Inc. v. Plough, Inc.*, 228 Md. 484, 180 A.2d 478 (1962). In *S.A.S. Personnel* and *G.E.M., Inc.* the Court of Appeals of Maryland analyzed the relationship between the Maryland statutes which require qualification or registration and Maryland Code, *Corporations & Associations Article*, § 7-301 (1975). Section 7-301 denies the right to sue in a Maryland court to a foreign corporation doing intrastate, interstate or foreign business in the State but which fails to comply with a registration or qualification requirement. In surveying applicable decisions through 1979, the Court of Appeals of Maryland, in *S.A.S. Personnel, supra*, at 286 Md. 339, 407 A.2d 1142, stated,

[5] *Corporations & Associations Article* of the Maryland Code §§ 7-203, 202 (1975).

> Foreign corporations which merely solicit orders or sales or engage in activities in Maryland directly related to such solicitation or sales, including the interstate delivery of goods, have, however, been held not to be 'doing business.'

Accordingly, the solicitation of interstate sales does not constitute "doing business" within the meaning of the registration or qualification statutes and a failure to qualify or register does not invoke the sanction barring prosecution of an action arising under the laws of the State of Maryland. *See Premier Industrial Corp. v. Nechamkin,* 403 F. Supp. 180 (D. Md. 1975); *accord, Gilliam v. Moog Industries, Inc.,* 239 Md. 107, 210 A.2d 390 (1965); *Champion Spark Plug Co. v. T.G. Stores, Inc.,* 356 F.2d 462, 463 (4th Cir. 1966); *United Merchants & Manufacturers, Inc. v. David & Dash, Inc.,* 439 F. Supp. 1078, 1087-89 (D. Md. 1977).

In affirming, the Court of Appeals for the Fourth Circuit found § 5-204 of the *Courts & Judicial Proceedings Article* of the Maryland Code "*in pari materia*" with the Maryland statutes analyzed by the Court of Appeals of Maryland in *S.A.S. Personnel* and *G.E.M., Inc.* Applying the same analysis, the court of appeals below concurred with the district court's appraisal of the uncontradicted evidence that Respondent's activities did not constitute "doing business" and that Respondent was, therefore, not required to register or qualify. As a result, the sanction prescribed by § 5-204 of the *Courts & Judicial Proceedings Article* of the Maryland Code for failing to register or qualify did not apply to bar Respondent's limitations defense.[6]

[6] Because § 5-204 of the *Courts & Judicial Proceedings Article* did not apply on its own terms to bar a limitations defense, the court of appeals below expressed no opinion as to that statute's applicability, if at all, to a federally created cause of action under the Securities Exchange Act of 1934. The appellate court did observe, however, that in referring to state statutes of limitations in claims under the federal Securities Exchange Act

III.

THE PROCEEDINGS BELOW IN THE DISTRICT COURT WERE PROPER IN EVERY RESPECT.

Petitioners attack the affirmance of three minor evidentiary rulings, the district judge's refusal to recuse himself after their pre-trial motion for his disqualification and the district judge's denial of a motion for new trial. Respondent, hereafter, will address each of the three issues in the order in which they are raised by Petitioners. Each attempt to have this Court review purely evidentiary and factual issues is without merit.

a. Evidentiary Rulings.

Applying Maryland law in this diversity action, the court of appeals below appropriately affirmed the admission into evidence of Petitioners' real estate and prior litigation experience as relevant to the question whether Petitioners rightfully relied upon the alleged misrepresentations. Under Maryland law, one of the five elements which had to be proven by Petitioners in their claims of common law fraud is justifiable reliance. *E.g., Wedeman v. City Chevrolet Co.*, 278 Md. 524, 532, 366 A.2d 7, 12 (1976). In pre-trial proceedings, Petitioners agreed that their prior litigation experience concerning septic systems was admissible. The reference at trial to the litigation matter now complained of was first put in issue by Petitioners, on direct examination, and inquired into on proper cross-examination under the close scrutiny of the district judge, in accordance with the safeguards of Fed. R. Evid. 403. The court of appeals approved the admission of such evidence as being well within the district court's discretion to permit relevant evidence on the question of justifiable reliance.

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of 1934, reference is only to the duration of time and not a "collateral" provision, such as § 5-204, "governing whether the statute of limitations shall apply." (Pet. App. p. 10).

Petitioners next contend they were deprived of the opportunity to introduce documents showing complaints about Respondent involving matters unrelated to the instant action and from persons not present at trial. The court of appeals found no error in the district judge's exclusion of such evidence, describing it as patent hearsay falling into none of the hearsay exceptions set forth in Fed. R. Evid. 803 (Pet. App. pp. 15-16). The exclusion of the documents was a straightforward application of the hearsay rule by the district judge.

Lastly, Petitioners again argue that since their prior litigation experience was admissible, they were automatically entitled to cross-examine a representative of Respondent on totally unrelated litigation. This the court of appeals below aptly described as Petitioners' "sauce-for-the-goose-sauce-for-the-gander argument" (Pet. App. p. 14). Respondent's cross-examination was proper on the issue of justifiable reliance; conversely, Petitioners' line of cross-examination had no basis of relevancy. The scope and extent to which cross-examination should go is within the sound discretion of the trial judge to safeguard against undue burdening of the record, or cumulative, irrelevant and prejudicial matters being placed before the jury. *E.g.*, *Glasser v. United States*, 315 U.S. 60 (1942); *Mannix v. United States*, 140 F.2d 250 (4th Cir. 1944); Fed. R. Evid. 403. Upon review of the record, the appellate court below characterized the unrelated litigation matters as "collateral" and "extraneous" (Pet. App. p. 14). Thus, the court of appeals cited two bases for its approval of the restriction on cross-examination: (1) to avoid irrelevant matters, Fed. R. Evid. 402, and (2) to avoid the confusion and prejudice of mini-trials of issues unrelated to the merits of the case, even had the matters possessed some attenuated relevance, Fed. R. Evid. 403.

b. PETITIONERS' MOTION TO DISQUALIFY DISTRICT JUDGE KAUFMAN.

Petitioners' motion to disqualify District Judge Kaufman was totally unfounded. The record below is devoid of any possible grounds on which to base an argument that the district judge was biased or prejudiced. Quite to the contrary, the record at trial below reflects the greatest latitude was given to Petitioners to enable them to present their case fully. The only extra-judicial grounds asserted in the motion to disqualify was an alleged incident when District Judge Kaufman was purportedly seen talking with one of the counsel for Respondent following a pre-trial hearing. Neither Judge Kaufman or Respondent's counsel recalled the alleged incident. (Appendix on Appeal to the Fourth Circuit vol. XIV pp. 4, 5).

The court of appeals below characterized Petitioners' claim that the district judge was in error in not disqualifying himself as "frivolous" (Pet. App. p. 16). Petitioners are now trifling with this Court's procedures in seeking review of the court of appeals' finding that District Judge Kaufman was totally correct in not disqualifying himself.

Disqualification of judges under either 28 U.S.C. § 144 (1949) or 28 U.S.C. § 455 (1974) requires that the alleged bias and prejudice stem from an extra-judicial source and result in an opinion on the merits on some basis other than what the judge learned from his participation in the case. *United States v. Grinnell Corp.*, 384 U.S. 563, 583 (1966). With respect to what appears to be the real reason for Petitioners' efforts to remove the district judge — adverse rulings — the court of appeals promptly disposed of that ground as insufficient for disqualification. *Ex Parte American Steel Barrel Co.*, 230 U.S. 35, 44 (1913).

The court of appeals below rejected Petitioners' basic premise that any contact between counsel and judge

outside the presence of the opposition during the pendency of a case is automatic grounds for recusal. Further, the court of appeals' review of the record found that Petitioners could not even establish that the alleged discussion between the district judge and counsel involved the case at bar. The decision on recusal is committed to the discretion of the district judge and is reviewable only if there exists abuse of sound judicial discretion. *United States v. Haldeman*, 559 F.2d 31 (D.C. Cir. 1976), *cert. denied*, 431 U.S. 933 (1977). The court of appeals below stated that Petitioners had established only their "belief" of impartiality, and nothing more. Finding not even the "hint" of abuse of judicial discretion (Pet. App. p. 22) by District Judge Kaufman in deciding not to recuse himself, the court of appeals properly affirmed.

c. Denial Of Motion For New Trial.

Only abuse of discretion by the trial judge in ruling on a motion for new trial will afford a basis for reversal on appeal. *E.g., Sloan v. Colebank*, 304 F.2d 668 (4th Cir. 1962). No abuse was present below.

The court of appeals (Pet. App. p. 22) and district judge below (Appendix on Appeal to the Fourth Circuit vol. II p. 1139) both stated that there was little conflict in the testimony. It was the jury's verdict, based on that testimony and upon proper instructions submitted without objection from Petitioners, that Petitioners did not carry their burden to establish any of the three frauds claimed. The Court of Appeals for the Fourth Circuit found that the record below clearly supported the jury's determination that Petitioners did not carry their burden. It necessarily followed that the appellate court found nothing to support even the inference of abuse of discretion in the district court's denial of the motion for new trial.

CONCLUSION

For the foregoing reasons, the Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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JUNE 16, 1980

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that three copies of the foregoing Brief of Respondent In Opposition were airmailed, postage prepaid, to Kenneth Leo Fowler and Flora D. Fowler, Petitioners, 137 Brandy Hills Drive, Port Orange, Flordia, 32019, this 16 day of June, 1980. I further certify that all parties required to be served have been served.

JOHN A. WOLF,
Attorney for Respondent.

APPENDIX

ORAL OPINION OF UNITED STATES DISTRICT JUDGE FRANK A. KAUFMAN GRANTING RESPONDENT'S MOTION FOR PARTIAL SUMMARY JUDGMENT DISMISSING PETITIONERS' SECURITIES FRAUD CLAIMS. (Taken from the Appendix on Appeal to the Court of Appeals for the Fourth Circuit Vol. IX pp. 84-90, proceedings in the District Court of Maryland of April 15, 1977).

Now I am going to the question of and orally rule on the motion for summary judgment on Count Two, and then I will come back to do scheduling with you, and reluctantly, and most reluctantly, Mr. Wolf, I am going to take a moment or two on these boilerplate damage standards.

Section 77b of Title 15 of the United States Code provides in part that the term "security" means any investment contract.

In the Howey case, the Supreme Court in 1946, 328 U.S. 293, faced the question of whether a somewhat different Florida land deal from the deal we have in this case was an investment contract.

In that case, the defendant sold small sections and seemingly in some instances individual rows of Florida citrus groves to out-of-state buyers attracted by promises of enormous profits. Agricultural management of the groves was only feasible on a large-scale basis. All of the purchasers signed management contracts in conjunction with their purchases. The vast majority of those contracts were with the defendant.

The Supreme Court held the arrangement was an investment contract and thus a security and the test that was stated was, in the words of Mr. Justice Murphy, writing for the majority of the Court — I am

not sure, maybe it was a unanimous Court. I am not quite clear and my notes here do not show. His words were: The test is whether the scheme involves an investment of money in a common enterprise, with profits to come solely from the efforts from others.

In United Housing Foundation v. Forman, 421 U.S. 837, 1975, Mr. Justice Powell considered whether shares in a New York cooperative housing project which entitled the purchasers to lease an apartment in the project were securities, and the Supreme Court held that those shares were not securities, largely because the primary purpose of the purchasers of those shares was to secure residential housing for themselves.

At page 852, referring to the Howey test, Mr. Justice Powell wrote: "This test, in shorthand form, embodies the essential attributes that run through all of the Court's decisions defining a security. The touchstone is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others."

In Forman at note 17 on page 853 of 421 U.S., there is a citation to an SEC release. That release applied by its terms to all types of units in real estate projects with the requisite characteristics set forth. That release deals primarily with condominium projects and after discussing the Howey test, the release states that under some conditions, an investment contract may be present in situations where an investor is not wholly inactive but even participates to a limited degree in the operations of the business, and certain examples are gone into.

That test is also referred to, that SEC release test, in footnote 16 in Forman, and there the Court noted that the test in Howey speaks in terms of profits to come solely from the efforts of others and goes on to say: "Although the issue is not presented in this case, we note that the Court

of Appeals for the Ninth Circuit has held that the word 'solely' should not be read as a strict or literal limitation on the definition of an investment contract, but rather must be construed realistically, so as to include within the definition those schemes which involved in substance, if not form, securities," and they cite to the Turner case in 474 F.2d, the Ninth Circuit case, and that cert. had been denied in that case by the Supreme Court.

I mistakenly said a moment ago that footnote 16 referred to the SEC release. That is not referred to until footnote 17 in Forman, but footnote 16 is talking about the same kinds of matters that come up in connection with the SEC release in the Ninth Circuit case.

The Supreme Court said as to the Turner point: "We express no view, however, as to the holding of this case," that is, the holding of Turner.

Now, Turner involved a get-rich-quick scheme by which members of the public bought the right to attend sales promotion meetings and to induce others to buy the same right. The investors participated in the scheme to the extent of inducing and tempting others to invest, and the type of transaction involved was not one in which the profit was to be derived solely from the efforts of others.

The Ninth Circuit, speaking through Judge Duniway, wrote: "We hold only that the requirement that profits come solely from the efforts of others would, in circumstances such as these, lead to unrealistic results if applied dogmatically, and that a more flexible approach is appropriate."

In Happy Investment Group v. Lakeworld Properties, Inc., 396 F. Supp. 175, Northern District of California, Judge Carter considered whether lots in a recreational subdivision were federal securities. He applied the Glenn Turner test of the Ninth Circuit and focused attention on the proposition that the defendants made essential managerial efforts which affected the success of the recreational subdivision.

Then at page 181, he went on to say: "Plaintiffs have tried to stress the passive nature of their investment; they have argued that the community could only come to fruition through the efforts of its promoter, Lakeworld. However, as plaintiffs admit, unless houses were built upon all those vacant lots, and people were attracted there to live, the projects would inevitably stagnate. In order for the community to develop, individual landowners had to build homes. House building cannot be considered a passive activity, requiring only a modicum of effort, as required by the Glenn Turner test."

In a Southern District of New York case in 1975, which is set forth at 401 F. Supp. 1045, the Davis case, the sale of unimproved land in a residential subdivision in New Mexico was contended to be a security.

The Court held there was no security and wrote at page 1050: "If defendants in fact built roads and other improvements, this is not the type of managerial service contemplated in Howey or United Housing. Defendants did not promise to run the development and distribute profits to the plaintiff, as did the operators of the orange groves in Howey. There was no management contract between plaintiff and defendants, nor were defendants obligated by the purchase agreement to perform any such services. Defendants' attempts to induce purchasers to build or their efforts, if any, to enhance living conditions in the development were unrelated to plaintiff. Their interest was in recouping their investment, making a profit and moving on. Any benefit to plaintiff would be purely incidental.

"In the absence of a common enterprise between the parties, the expectation of a profit on resale is insufficient to transform what is essentially a sale of real property into the sale of an investment contract," and so forth.

I think the case law to date indicates that each new scheme must be looked at on its own, just as the cases I have cited indicate, and that general summary is the law as stated by the foremost authority in the field, Professor

Loss, at 1 L. Loss, Securities Regulation 490, Second Edition, 1961, Volume 1.

I think the file in this case reveals undisputedly that the sale of real estate involved in this case did not involve the sale of any security. The extent to which plaintiffs themselves participated in site location and plans for building a house on one or more of their lots takes the case out of the "efforts of others" requirement, even under the liberal approach of the Ninth Circuit in Turner, which the Supreme Court stated it was not taking a position on in its footnote comment in Forman.

The plaintiffs rely on several cases, including a District of Minnesota case at 340 F. Supp. 1318, and a Tenth Circuit case in 1975, 527 F.2d 204. The first case is SEC v. Lake Havasu Estates. That is the Minnesota case. The other case in the Tenth Circuit is the McCown case. I do not think there is anything in those cases that teaches to the contrary of what I have indicated I believe the law to be.

For the reasons that I have stated, the motion for summary judgment as to Count Two is granted. That in no way affects what we do under Count One.